

# Exam Strategies

The following Q & A can be helpful in preparing for the HKCE Economics Examination:

## Q *What should I pay attention to in doing Paper 1?*

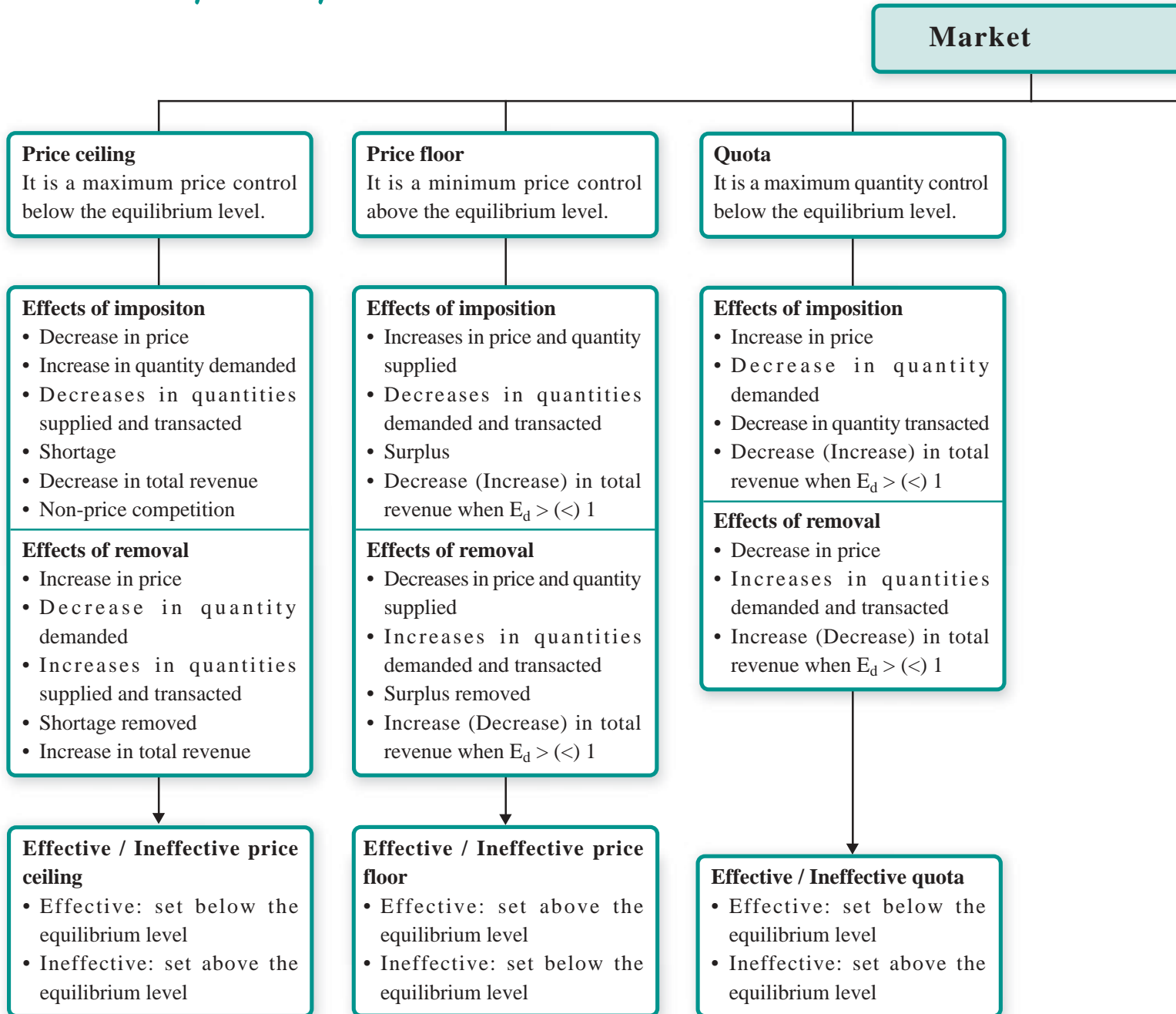
- A
- Read the questions carefully.
  - Look for the question commands, for example: define, state, find, point out, what is, list, identify, indicate, show, suggest, explain, give reason(s), give example(s), draw, distinguish, compare and calculate, ect.
  - Circle or highlight the important words and key information in the questions.
  - Do not rush to answering the questions without understanding what the questions really ask.
  - Do not write unnecessary long answers with empty content. Students may refer to the mark of each question to determine the appropriate length of answers.
  - Avoid using arrows or non-standardised symbols in the verbal answer.
  - Mind the handwriting.
  - Leave some blank lines between the answers to different questions.
  - Do not attempt to write down all materials prepared or learnt in lessons. Always aim at directly answering the question with explanation.
  - Do not overuse time in each question so that the time spent on each question is proportional to its mark.
  - No need to start a new page for **EACH** question in Section A.
  - For Section B, start each full question (not part of a question) on a new page.

## Q *What should I pay attention to in drawing diagrams?*

- A
- The diagrams should be properly sized, i.e. not too big nor too small.
  - Use pencil instead of pen.
  - Use ruler in drawing straight lines.
  - Label the axes properly without error.
  - Label the lines and curves properly.
  - Use lines to indicate and label the quantity or price level which are relevant in the explanation.
  - Use arrow(s) to show the direction of relevant change.
  - Make sure that the diagram drawn is clear, tidy and neat for the marker to read.

# 5 Market Intervention

## Concept Map



## Intervention

### Tax (Per-unit and *ad valorem*)

#### Effects

- Decrease in supply
- Increase in price
- Decrease in quantity transacted
- Total tax burden  
= Per-unit tax × New quantity transacted
- Consumers' tax burden  
= Change in price × New quantity transacted
- Producers' tax burden  
= Total tax burden – Consumers' tax burden

#### Share of tax burden

- If  $E_d > E_s$ , Consumers' < Producers' tax burden
- If  $E_d < E_s$ , Consumers' > Producers' tax burden

#### Extreme cases

	P	$Q_t$	Tax burden
$E_d = \infty$	No change	Decrease	Producers
$E_d = 0$	Increase	No change	Consumers
$E_s = \infty$	Increase	Decrease	Consumers
$E_s = 0$	No change	No change	Producers

### Subsidy (Per-unit and *ad valorem*)

#### Effects

- Increase in supply
- Decrease in price
- Increase in quantity transacted
- Total subsidy benefit  
= Per-unit subsidy × New quantity transacted
- Consumers' subsidy benefit  
= Change in price × New quantity transacted
- Producers' subsidy benefit  
= Total subsidy benefit – Consumers' subsidy benefit

#### Share of subsidy benefit

- If  $E_d > E_s$ , Consumers' < Producers' subsidy benefit
- If  $E_d < E_s$ , Consumers' > Producers' subsidy benefit

#### Extreme cases

	P	$Q_t$	Subsidy benefit
$E_d = \infty$	No change	Increase	Producers
$E_d = 0$	Decrease	No change	Consumers
$E_s = \infty$	Decrease	Increase	Consumers
$E_s = 0$	No change	No change	Producers

## Learning Focus

- Interpret nominal and relative prices.
- Distinguish between demand and quantity demanded, and between supply and quantity supplied.
- Perform horizontal summation to obtain market demand curve and market supply curve.
- Explain the relationship between quantity demanded, quantity supplied and quantity transacted.
- Describe some aspects of market equilibrium and disequilibrium.
- Predict the change in price when the market is in disequilibrium.

## 2.1 Nominal price and relative price

- Price is an **exchange ratio between goods**. It can be expressed in nominal or relative term.
- The nominal price (名義價格) of a good is **expressed in terms of money**.
  - For example, the price of a can of coke is \$5, and the price of a cup of coffee is \$20.
- The relative price (相對價格) of a good is **expressed in terms of another good forgone**.
  - For example, the price of a can of coke is 0.25 cup of coffee, and the price of a cup of coffee is 4 cans of coke.

### Reminder

The relative price of a good also shows the opportunity cost of buying the good.

### Progress Checkpoint 1

If the nominal price of a cup of coffee falls to \$10 while that of a can of coke is still \$5, what are the relative prices of:

- a cup of coffee in terms of coke; and
- a can of coke in terms of coffee?

#### Suggested Answer

- (a) The relative price of a cup of coffee in terms of coke:

$$\frac{\$10}{\$5} = 2 \text{ cans of coke}$$

- (b) The relative price of a can of coke in terms of coffee:

$$\frac{\$5}{\$10} = 0.5 \text{ cup of coffee}$$

## B. Change in demand

Price (\$)	Old $Q_d$ (units)	Increase in demand	Decrease in demand
		New $Q_d$ (units)	New $Q_d$ (units)
1 000	120	200	40
800	160	240	80
600	200	280	120
400	240	320	160
200	280	360	200

Table 3.2 Changes in demand

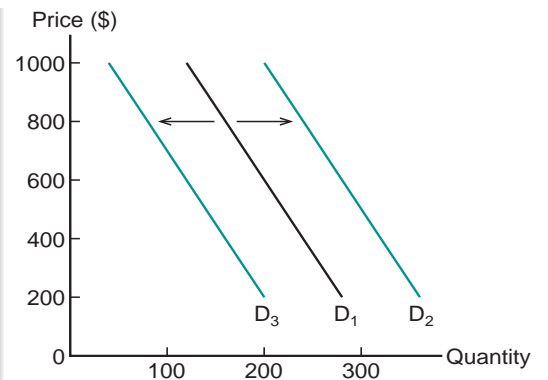


Figure 3.2 Changes in demand

### (a) Increase in demand

- When consumers plan to buy 80 more units of good at every price level, the whole demand schedule changes as shown in the column labelled ‘Increase in demand’ in Table 3.2.
- This increase in demand is also shown by a rightward shift of demand curve from  $D_1$  to  $D_2$  in Figure 3.2.

### (b) Decrease in demand

- When consumers plan to buy 80 fewer units of good at every price level, the whole demand schedule changes as shown in the column labelled ‘Decrease in demand’ in Table 3.2.
- This decrease in demand is also shown by a leftward shift of demand curve from  $D_1$  to  $D_3$  in Figure 3.2.



### Reminder

A change in demand is caused by a change in the factors affecting demand EXCEPT price.

## C. Factors affecting demand

### (a) Prices of related goods

#### (i) Substitute goods

- Two goods are substitutes (代替品) or in competitive demand (競爭需求) **if one can easily replace another in satisfying human wants.**
- For example, if the price of LCD monitors decreases, the demand for CRT monitors will decrease.

#### (ii) Complementary goods

- Two goods are complements (輔助品) or in joint demand (聯合需求) **if they are used together in satisfying human wants.**
- For example, if the price of DVD players decreases, the demand for DVDs will also increase.



Figure 3.3 DVD player and DVDs

## Concept Explorer 2.1

### Equilibrium and disequilibrium

A market is either in equilibrium or disequilibrium, depending on the level of the market price. Consider the following table:

Price (\$)	Quantity demanded (units)	Quantity supplied (units)	Equilibrium / Disequilibrium	Quantity bought (units)	Quantity sold (units)	Change in price
2	95	25	Disequilibrium (shortage of 70 units)	25	25	Increase
10	15	85	Disequilibrium (surplus of 70 units)	15	15	Decrease
6	55	55	Equilibrium	55	55	Remain constant

Table 2.8

- Since the buyers can buy and the sellers can sell the quantity they want at \$6, the price has no tendency to change. The market is in equilibrium.
- The market price of \$6 is the equilibrium price, while the quantity transacted of 55 units is the equilibrium quantity.

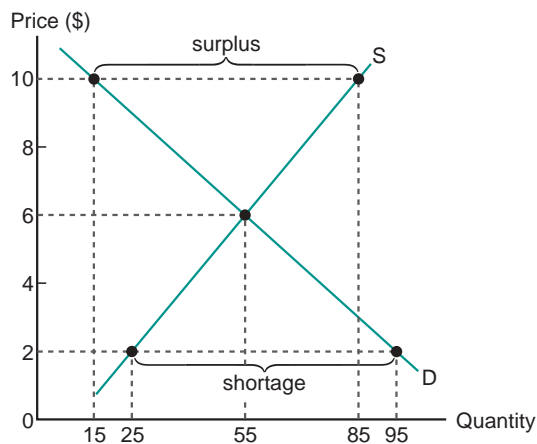


Figure 2.7 Market equilibrium and disequilibrium



**Reminder**  
When the market is in equilibrium, there is no shortage or surplus.

### Progress Checkpoint 4

Refer to the following market demand and supply schedules:

Price (\$)	100	200	300	400	500
Quantity demanded (units)	160	135	110	85	60
Quantity supplied (units)	72	91	110	129	148

Table 2.9

Price (\$)	Quantity demanded (units) in a month of				Quantity demanded (units) in a month in the market
	A	B	C	D	
10	5	2	3	5	15 (= 5 + 2 + 3 + 5)
8	10	4	8	13	35 (= 10 + 4 + 8 + 13)
6	15	6	13	21	55 (= 15 + 6 + 13 + 21)
4	20	8	18	29	75 (= 20 + 8 + 18 + 29)
2	25	10	23	37	95 (= 25 + 10 + 23 + 37)

Table 2.2 Individual and market demand schedules

Price (\$)	Quantity demanded (units) in the market
10	15
8	35
6	55
4	75
2	95

Table 2.3 A market demand schedule

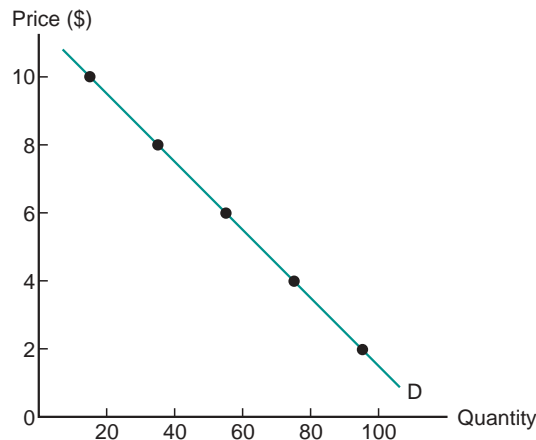


Figure 2.2 A market demand curve

## D. The law of demand

- A demand curve is normally downward sloping, due to the law of demand (需求定律) .
- The law of demand states that: **If the (relative) price of a good decreases, its quantity demanded will increase, vice versa (反之亦然) ; *ceteris paribus*.**



### Reminder

The law of demand simply implies that people buy more of a good when it is cheaper, and vice versa.

## Theory in Life 2.1

### The law of demand and clearance sales

The general manager of a department store wants to increase sales. Different strategies such as advertisement on TV and lucky draw are considered. He eventually decides to offer 70% discount on all items. Can you tell the rationale behind his choice?

#### Solution

The general manager understands that customers act according to the law of demand. If he reduces the prices of the items sold in his store, the quantities demanded of them will rise. This will help to increase sales.



Figure 2.3 Clearance sales

- Macroeconomics (宏觀經濟學) is the study of an economy as a whole. Outputs are aggregated and the whole economy is analyzed from various aspects, such as total output, price level, employment, money and banking, public finance, trade and balance of payment.

## Glossary

capital good	資本物品	the good used by producers to assist the production of other goods
consumer good	消費物品	the good used by consumers to directly satisfy human wants
economic good	經濟物品	the good whose quantity available is insufficient to satisfy all wants for it
factor market	生產要素市場	the market wherein factor services are traded between firms and households
firm	廠商	the production unit which produces and sells goods and services to households for revenue
flow concept	流量	the variable measured per time period
free good	免費物品	the good whose quantity available is sufficient to satisfy all wants for it
good	物品	anything which provides satisfaction
household	家庭	the consumption unit which pays expenditure to buy goods and services from firms
macroeconomics	宏觀經濟學	the study of an economy as a whole
market economy	市場經濟	the economy wherein resource allocation are determined by price mechanism
microeconomics	微觀經濟學	the study of how individual firms and households make decisions on production and consumption, and how scarce resources are allocated in a market economy
opportunity cost	機會成本	the highest-valued option forgone (resulting from an act)
planned economy	計劃經濟	the economy wherein resource allocation are determined by government decisions
price mechanism	價格機制	the use of price to allocate scarce resources
product market	產品市場	the market wherein final outputs are traded between firms and households
scarcity	稀少性	the situation wherein the quantity available of a good is insufficient to satisfy all wants for it
stock concept	存量	the variable measured at a particular point of time



## Exam Question Analysis

### Exam Question Distribution

Topics	Short and Structured Questions (Year)	Multiple-choice Questions (Year)
Scarcity and choice	—	94 (1), 95 (1,2), 97 (1), 98 (1, 54), 99 (1)
Opportunity cost	95 (B: 10ai), 96 (A: 1), 97 (B: 11b), 98 (A: 1), 99 (A: 1), 01 (B: 10d), 02 (B: 10c), 03 (B: 11bi)	94 (2, 3, 14), 95 (5), 96 (1,2), 97 (2, 49), 98 (3, 50), 99 (1, 50), 00 (2, 53), 01 (1), 02 (2, 3, 4), 03 (2)
Economic and free goods	94 (A: 1), 00 (A: 1), 02 (A: 1)	95 (3), 96 (55), 97 (12), 98 (2, 53), 99 (2), 00 (1, 47), 01 (47), 02 (1, 2), 03 (1)
Consumer and capital goods	—	94 (15), 95 (14), 96 (2), 99 (10)
Solving the problems of resource allocation	96 (B: 10d)	94 (4, 5), 95 (20), 96 (3), 97 (4), 98 (4), 99 (3, 37), 00 (4), 01 (2), 02 (5), 03 (4)

### Errors and Improvement

Wrong concepts / Common errors	Correct concepts
<p><u>On scarcity</u></p> <ol style="list-style-type: none"> <li>Fixed in supply implies scarcity.</li> <li>Richness can get rid of scarcity.</li> </ol>	<p><u>On scarcity</u></p> <ol style="list-style-type: none"> <li>Scarcity is a relative concept. Fixed supply does not necessarily imply scarcity.</li> <li>So long as wants are unlimited and resources are insufficient to satisfy them, scarcity exists.</li> </ol>
<p><u>On opportunity cost</u></p> <ol style="list-style-type: none"> <li>Cost is the alternative forgone / next best alternative forgone / all options forgone.</li> <li>A lower value of the chosen option implies a higher cost.</li> <li>A change in the value of the highest-valued option forgone will not change the cost.</li> <li>The cost of using one's own premises is zero.</li> <li>One option represents one good.</li> <li>Time or money itself is cost.</li> <li>Mix up accounting cost with economic cost.</li> </ol>	<p><u>On opportunity cost</u></p> <ol style="list-style-type: none"> <li>Cost is the highest-valued option forgone, not all options forgone.</li> <li>A lower value of the chosen option has no effect on the highest-valued option forgone.</li> <li>A rise (fall) in the value of the highest-valued option forgone implies the cost is higher (lower).</li> <li>So long as there is an option of renting the premises out to earn a rent, opportunity cost arises.</li> <li>One option can be a combination of more than one good.</li> <li>Time or money itself is not cost. Only the highest-valued alternative use of time or money is cost.</li> <li>Accounting cost without any option forgone is not cost in economics.</li> </ol>

# Demonstration

## Paper I Short and Structured Questions

### Section A

1. (a) What is price? (2 marks)

(b) If the nominal price of Good X is higher, on what condition can we say that it is cheaper? (3 marks)

#### Guidelines

This question is related to relative price. Hence, students should not answer by simply saying that nominal price decreases.

#### Suggested Answer

(a) Price is the exchange ratio between goods. 1  
It can be expressed in nominal and relative prices. 1

(b) If the proportionate increase in the nominal price of Good X is smaller than that of another good, 2  
its relative price will be lower, and we can say that it is cheaper. 1

2. (a) What does the law of demand state? (2 marks)

(b) On what condition is quantity demanded different from quantity bought? Explain. (3 marks)

#### Guidelines

- It refers to either the condition of surplus, shortage or equilibrium.
- Students need not consider those conditions on which quantity demanded and quantity bought are the same.

#### Suggested Answer

(a) The law of demand states that if (relative) price decreases, quantity demanded will increase, vice versa: *ceteris paribus*. 2

(b) Quantity demanded is the amount of a good a person is willing and able to buy at a particular price level, given the plan of purchase. 1  
Quantity bought is the amount of a good that has actually been purchased by buyers in the market. 1  
On the condition of shortage, quantity bought is less than quantity demanded. 1

#### Guidelines

Students should firstly provide the definitions of quantity demanded and quantity bought.

3. Some convenience stores sell lunch boxes at a low price. This attracts a large number of people to buy, but not all consumers' demand for the lunch boxes are satisfied. Explain this phenomenon with the aid of a diagram. (5 marks)

#### Guidelines

This shows that the market is not in equilibrium.

#### Guidelines

Students are asked to explain the phenomenon, not to predict the change in price.

Suggested Answer

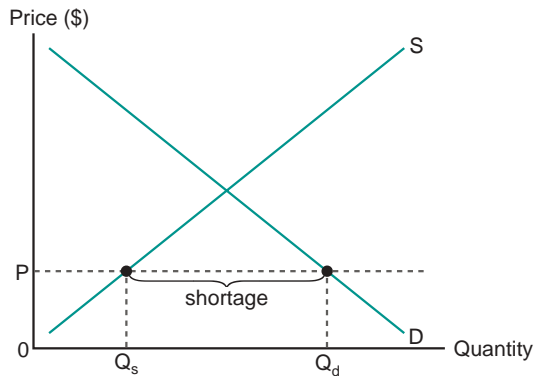


Figure 2.12

 Guidelines

- 1 mark is for the market price set below the equilibrium level.
- 1 mark is for the shortage.

2

- If the market price of the lunch boxes ( $P$ ) is set below the equilibrium level, the quantity demanded ( $Q_d$ ) will be greater than the quantity supplied ( $Q_s$ ). 1
- A shortage will arise. 1

**Section B**

4. (a) (i) The price of automobiles has recently decreased. The following are the responses of two persons:

Simon: 'Cars are cheaper now. I plan to buy one more for my wife.'

Paul: 'My family has already bought a car. I don't think I will buy more just because they are cheaper.'

 Guidelines

Students should check which response conforms to the law of demand.

Who acts according to the law of demand? Explain.

(2 marks)

 Guidelines

It is related to the conditions of market equilibrium and disequilibrium.

(ii) When people act according to the law of demand, the market will be in equilibrium. Do you agree? Explain.

(3 marks)

(b) Consider the following demand and supply schedules:

Price (\$)	100	200	300	400	500	600	700
$Q_d$ (units)	3 400	3 200	3 000	2 800	2 600	2 400	2 200
$Q_s$ (units)	1 000	1 400	1 800	2 200	2 600	3 000	3 400

Table 2.10

# Practice

## Paper I Short and Structured Questions

### Section A

- State the law of supply. (2 marks)
  - Explain the difference between quantity supplied and quantity sold. [Hint 1](#) (3 marks)
- Director: 'Why is there unsold clothing in our warehouse?'

Manager: 'This is because the price is set too high.'

Use a well-labelled supply-demand diagram to explain what the manager means. [Hint 2](#) (6 marks)

### Section B

- The following table shows the demand schedules of Consumers A, B, C and D for Good X in a period:

Price (\$)	Quantity demanded (units) of			
	A	B	C	D
500	100	30	70	50
400	110	60	90	100
300	120	90	110	150
200	130	120	130	200
100	140	150	150	250

Table 2.13

Find the quantity demanded at each price level in the market. [Hint 3](#) (2 marks)

- The following table shows the supply schedules of Sellers E, F, G and H for Good X in the same period:

Price (\$)	Quantity supplied (units) of			
	E	F	G	H
500	200	100	200	100
400	190	85	180	80
300	180	70	160	60
200	170	55	140	40
100	160	40	120	20

Table 2.14

Find the quantity supplied at each price level in the market. [Hint 4](#) (2 marks)

- Draw the market demand and supply curves. (2 marks)
- What are the equilibrium price and quantity? In your diagram, draw two dotted lines to show **EACH** of them. [Hint 5](#) (4 marks)

# Index

<b>A</b>			
<i>ad valorem</i> subsidy 從價津貼	121	entrepreneur 企業家	162
<i>ad valorem</i> tax 從價稅	117	equilibrium 均衡	33
arc elasticity of demand 弧需求彈性	80	equilibrium price 均衡價格	33
arc elasticity of supply 弧供給彈性	90	equilibrium quantity 均衡數量	33
average cost 平均成本	193	external growth 外部擴張	234
average labour productivity 勞工平均生產力	146, 165	<b>F</b>	
average product 平均產量	187	factor market 生產要素市場	13
<b>B</b>		factors of production 生產要素	162
basic salary plus commission 底薪加佣金	167	firm 廠商	13, 212
bonds / debentures 債券	217	fixed cost 固定成本	192
<b>C</b>		fixed factor 固定生產要素	186
capital 資本	162	flow 流量	14
capital accumulation 資本累積	163	free good 免費物品	9
capital consumption 資本消耗	163	<b>G</b>	
capital depreciation 資本折舊	163	general partnership 普通合夥	213
capital formation 資本形成	163	geographical mobility 地域流動性	173
capital good 資本物品	11	good 物品	9
cartel 同業聯盟	234	<b>H</b>	
<i>ceteris paribus</i> 其他因素不變	29	heterogeneous products 異質產品	251
competitive demand 競爭需求	53	homogeneous products 同質產品	251
competitive supply 競爭供給	58	horizontal integration 橫向合併	235
complementary good 輔助品	53	household 家庭	13
conglomerate integration 集團整合	235	<b>I</b>	
consolidation 合併	234	inelastic demand 低彈性需求	81
consumer good 消費物品	11	inelastic supply 低彈性供給	90
<b>D</b>		inferior good 劣等物品	54
demand 需求	29, 53	input 投入	142
demand curve 需求曲線	29	interest 利息	172
demand schedule 需求表	29	internal growth 內部擴張	234
derived demand 引申需求	54	<b>J</b>	
diseconomies of scale 規模不經濟	195	joint demand 聯合需求	53
division of labour 分工	146	joint supply 聯合供給	59
<b>E</b>		<b>L</b>	
economic good 經濟物品	9	labour 勞工	146
economies of scale 規模經濟	195	land 土地	162
elastic demand 彈性需求	81		
elastic supply 彈性供給	90		